

# ***Research on the Restrictive Factors of Establishing Cross-straits Common Market***

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**Abstract:** The establishment of the cross-Straits common Market was first proposed at the beginning of this century and has repeatedly appeared in official government documents. So far, however, progress on the common market has been slow. Therefore, this paper mainly studies the restricting factors of cross-strait common market. This paper first analyzes the status of the common market in the process of economic cooperation. Then it analyzes the current situation of cross-strait cooperation through trade, investment, industrial layout and Preferential Taiwan policies. Finally, we find that political opposition, structural contradiction and political opposition are the restrictive factors for the establishment of cross-Straits common market.

**Keywords:** cross-strait, common market

## **1. Introduction**

### **1.1. Background**

At the meeting commemorating the 40th anniversary of the Message to Compatriots in Taiwan, China president Xi Jinping pointed out that "we will actively promote the institutionalization of cross-Straits economic cooperation, build a cross-Straits common market, and strengthen the economy of the Chinese nation." At the same time, the Outline of the 14th Five-Year Plan (2021-2025) for National Economic and Social Development and Vision 2035 of the People's Republic of China put forward that "strengthening cross-Straits industrial cooperation, building cross-Straits common market, and expanding the national economy". Therefore, it can be seen that establishing the common market of cross-Straits has become one of China mainland's leading policies towards Taiwan China.

The cross-Straits Common Market was first proposed by Vincent Siew, a well-known Taiwanese politician, in 2001. The real implementation of this policy was announced in the 2005 Lian Hu Communiqué signed by the Kuomintang and the Communist Party of China, in which "cross-strait" refers to the Chinese Mainland and Taiwan. Additionally, the Cross-Straits Common Market Foundation has been established as a private consortium to construct the economic integration of and improve the economic development of the cross-straits. Therefore, it has been nearly 20 years since the proposal of the Cross-Straits Common market, but the progress of the common market is plodding. This paper tries to analyze the current situations of cross-Straits economic cooperation and research the restrictive factors of establishing a cross-Straits common market.

## 1.2. Research Question and Main Argument

At the 17th CPC National Congress held in October 2007, "peaceful development" was officially adopted as the theme for the new generation of CPC Central Leadership to promote cross-strait relations. In addition, after Ma Ying-jeou took power in May 2008, he proposed that the cross-straits must sign the Comprehensive Economic Cooperation Agreement (CECA) to promote the normalization of cross-strait economic relations [1]. Also, in June 2010, the Economic Cooperation Framework Agreement (ECFA) was formally signed. However, in the ten years since the signing of ECFA, despite the deeper economic and trade cooperation between the cross-straits, no further official documents have been signed. In addition, due to the influence of the Taiwan sunflower movement, the ECFA service trade agreement negotiations have been put on hold until now. Therefore, in this paper, I will argue that there is a political confrontation between the strait. Also, I argue that the cross-strait exist structural contradictions economic relations. Finally, I believe that Although the ECFA has been signed, the cross-strait still lack institutional safeguards. Therefore, this paper will try to argue the three arguments.

## 1.3. Structure of Paper

This paper will include five sections. In the next section, the definition of common market will be proposed through reviewing the different stage of economic cooperation. In the third part, I will analyze the current situation of cross-straits economic cooperation through trade, investment and preferential policies on Taiwanese. In the fourth parts, I will talk about the restrictive factors of the establishment of economic cooperation. In the final part, I will summarize the all paper and propose the limitations of this paper.

## 2. The Definition of Common Market

The common market is an advanced stage of regional economic integration. It characterized by the elimination of tariffs and quantitative restrictions on commodity trade among members of regional cooperation, the free flow of production factors (capital, labor, etc.) within the region, and the imposition of uniform tariffs on goods imported from non-members [2]. In addition, according to the complexity of regional resources and the differences in the degree of integration, the academic circle divides the organization forms of economic integration into six types: preferential tariff area, free trade area, customs union, common market, economic and monetary union, and complete economic integration [3].

### 2.1. Preferential Trade Agreements

Preferential Trade Arrangements (PTA) is the lowest and loosest form of economic integration, requiring members to lower tariffs on some or all products in the region by agreement such as preferential Trade Area of Africa. Since this preferential trade arrangement only partially eliminates the trade discrimination before the integration, it is a harmful and imperfect regional economic integration organization. Therefore, the ECFA is still in this state.

### 2.2. Free Trade Area

Free Trade Zone (FTA) refers to an economic and trade agreement or treaty reached by two or more countries or regions. It can eliminate reciprocal tariffs and other trade barriers and measures related to tariffs, thus forming an international economic integration organization. For example, the North American Free Trade Area (NAFTA), and the Regional Comprehensive Economic Partnership

(RCEP) are free trade zones. However, the walls to the free flow of factors of production in the free trade zone have not been completely eliminated.

### **2.3. Customs Union**

Customs union (CU) is a higher form of integration than free trade. Tariff and non-tariff barriers of all member countries are required to eliminate in the region and also adopts uniform tariffs on non-member countries. The most famous CU in history is the Benelux, which consists of Belgium, Luxembourg, and the Netherlands.

### **2.4. Common Market**

The common market not only includes the content of CU but also realizes the free flow of factors of production in the region. additionally, it also unified the monetary system and stipulated the range of exchange rate fluctuation of each member. The model of the common market was the European Community.

### **2.5. Economic Union**

Economic Union (EU) realizes the free flow of goods and production factors. It forms the consistent coordination between fiscal and monetary policies and other economic policies (industrial policies, agricultural policies, etc.). As an advanced form of integration, the EU requires members to transfer part of their powers to the community, which is difficult to achieve. At present, only the European Union has reached this stage in the world.

### **2.6. Complete Economic Integration**

Complete economic integration (CEI) from the EU is the highest form of economic integration. It requires members in trade, fiscal, monetary, and other economic policy to fully agree, not only between members, to realize the full integration of the goods and production factors and form a super-sovereign institution for unified management. CEI is complicated because it requires the members to cede all economic sovereignty and political power. So far, no regional economic integration organization has fully met this criterion. The European Union has begun to take its basic form. However, with the Brexit of the United Kingdom and the disagreement among its members, the European Union integration process has experienced significant setbacks. Its development prospect remains to be further observed.

Therefore, the common market belongs to the advanced stage of regional economic integration. The core of the common market theory is to form a large transboundary market by realizing free trade and the free flow of factors within the region. Therefore, the common market can not only promote free trade and free flow of production factors, but also improve the productivity through expanding the production borders, which can increase social welfare within the region

At present, the cross-straits are still in the FTA stage, and there is no other development trend. Therefore, it is necessary to research the limiting factors of the development of common market of cross-Strait.

## **3. The Current Situation of Cross-strait Common Market**

ECFA is the first cross-strait's institutional economic cooperation agreement. The signing and implementation of ECFA will positively impact promoting economic and trade cooperation between China mainland and China Taiwan. Therefore, it is necessary to analyze the current situation of economic cooperation between two sides after the signing of the ECFA.

### 3.1. Cross-strait Trade Has Grown Steadily

After signing ECFA, cross-strait trade shows a rising trend. According to the General Administration of Customers P.R China [4], the total volume of imports and exports across the straits increased from \$106.23 billion in 2009 to \$260.81 billion in 2020, with an average annual growth rate of 7.9 percent, and exceeded \$250 billion in 2020. According to the 2021 China Import Development Report [5] jointly released by the School of Economics and Business Administration of Beijing Normal University and the China Institute of Education and Social Development, Taiwan was the China mainland's largest source of imports in 2020, accounting for 9.76% of the total imports of the Chinese mainland, with imports from Taiwan reaching 2000.6 billion US dollars. Additionally, China is Taiwan's most significant trading partner. Taiwan's economic dependence on the mainland is increasing year by year. the mainland is the largest export market and source of Taiwan's largest trade surplus. According to data from the General Administration of Customers P.R China [4] (See Figure 1), the import and export volume between the Mainland and Taiwan in 2020 was \$260.81 billion, an increase of 88.1% over 2009, accounting for 24.3% of Taiwan's total foreign trade. Taiwan's exports to the Mainland reached \$20.66 billion, of which early harvest products accounted for 21.6% of Taiwan's total exports to the Mainland. Taiwan imported \$60.14 billion from the Mainland, and its trade surplus with the Mainland was \$140.52 billion, accounting for 79.2% of Taiwan's overall trade surplus. On the whole, Cross-straits trade has developed rapidly, and the mainland remains an important source of Taiwan's trade surplus

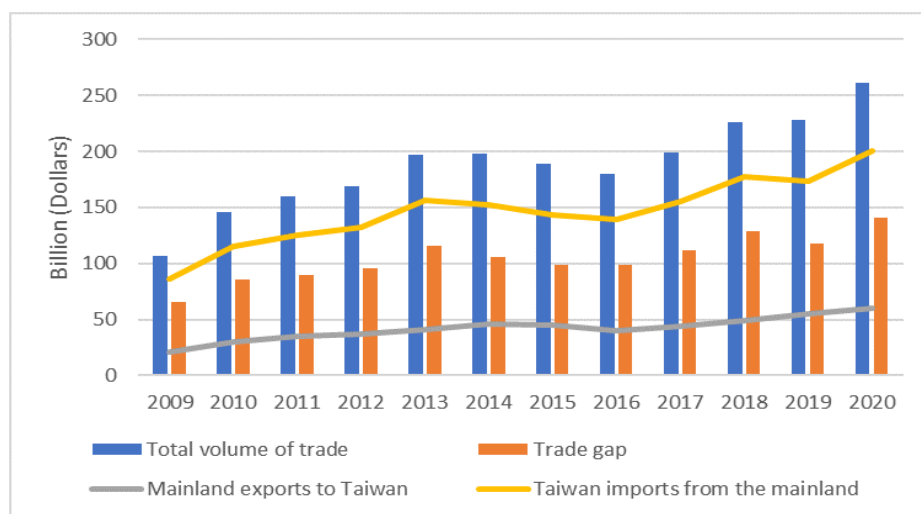


Figure 1: Cross-strait trade development from 2009 to 2019.

### 3.2. The China Mainland has Become Taiwan's Largest Overseas Investment Destination

After signing and implementation of the ECFA, the cross-straits have an institutionalized cooperation, and Taiwan's investment in the Mainland has grown steadily. According to statistics from the Ministry of Economic Affairs [6] (Republic of China), by the end of 2020, more than 50% of Taiwan's outbound investment flowed to the Mainland, with the total investment reaching \$192.42 billion. In recent years, the proportion of Taiwan's investment in the Mainland in its total outbound investment has decreased slightly, but it is still at a high level of around 33% (see Figure 2). China has been Taiwan's most prominent destination for overseas investment for an extended period. In addition, According to statistics from the General Administration of Customers P.R China [4], by the end of 2020, the Mainland had used us \$70.4 billion of Taiwan's investment, accounting for 3.1 percent of

the Mainland's total overseas investment. Considering Taiwan businesses' reinvestment in the Mainland through third places, the Mainland has used over \$130 billion of Taiwan's capital [7].

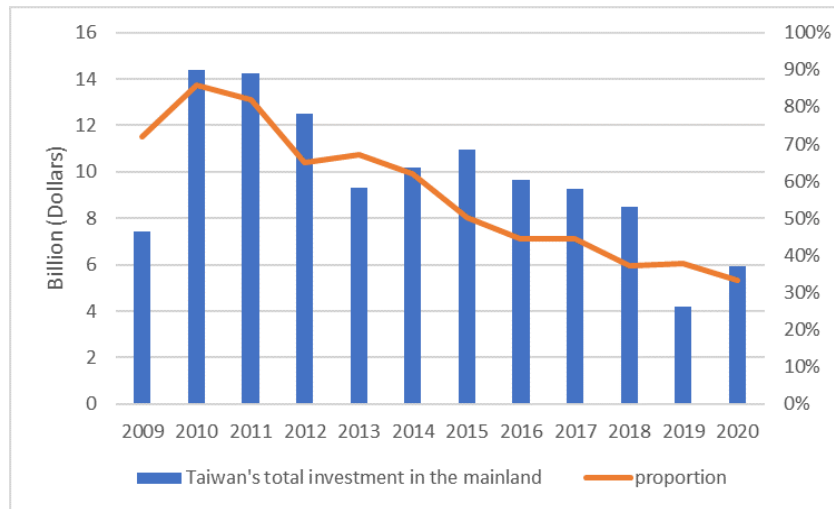


Figure 2: Taiwan's investment in the China Mainland from 2009 to 2020.

### 3.3. The Amount of China Mainland Investment in Taiwan Fluctuates

In 2008, after the positive development of cross-strait relations, the cross-straits decided to implement the policy of "tightening first, broadening later," "gradual progress," and "achievements then expanding." Taiwan opened mainland investment to Taiwan on June 30, 2009, allowing mainland investment to set up subsidiaries, branches, or offices in Taiwan in direct or indirect investment. Then, in 2011 and 2013, some new investment sectors were opened up. However, mainland enterprises are not familiar with Taiwan's industrial environment and relevant rules and regulations due to the short opening period, so the amount of investment in Taiwan is not large, and most mainland investors are still exploring the Taiwan market. Unfortunately, since the Democratic Progressive Party (DPP) took power on May 20, 2016, the Taiwan authorities have often adopted various ways to restrict mainland investment in Taiwan and mainland employees' visits to and from the Mainland. In addition, statistics from the Mainland show that as of June 2020, a total of 516 non-financial companies from the Mainland had established enterprises or representative offices in Taiwan with a record amount of \$2.78 billion, covering wholesale and retail, communications, plastic products, tourism and other industries, accounting for only a fraction of the total OFDI from the Mainland.

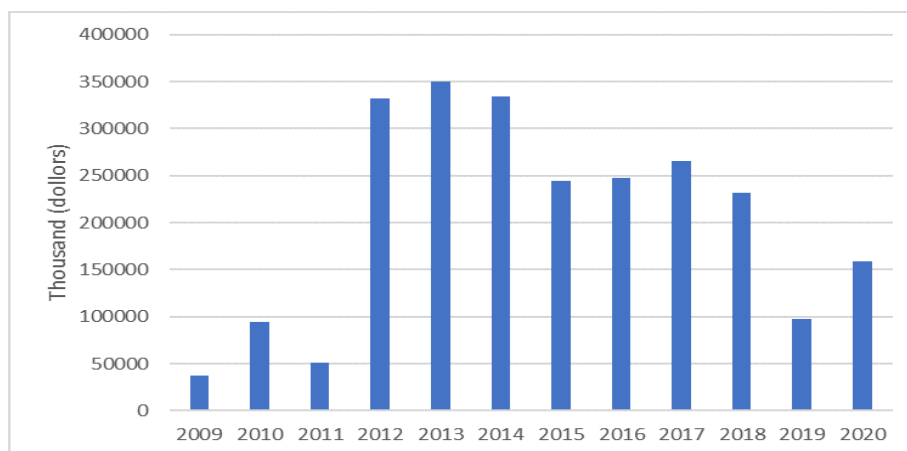


Figure 3: Mainland investment in Taiwan from 2009 to 2020.

### **3.4. Taiwan's Industrial Layout in the China Mainland Is Increasingly Optimized**

Mainland China has enormous market potential, economic solid scale effect, complete industrial system, and gradient depth of development in the east, middle, and west. It has vast complementary advantages with Taiwan's highly export-oriented economic form and partial industrial competitiveness. In the early stage, Taiwan's exports to Mainland China were mainly labor-intensive products, particularly necessities. After 2000, the structure of commodity trade between Mainland and Taiwan began to undergo significant changes, and the design of Taiwan's export commodities to Mainland changed from the original labor-intensive to technology and capital-intensive [8]. Taiwan's investment activities in the Mainland are mainly based on its manufacturing advantages and the labor cost and market advantages of the Mainland, so the industries invested in the Mainland are especially manufacturing, primarily electronic, optical products and their components [9]. In terms of region, in recent years, the eastern part has seen rising production costs and insufficient labor supply. The central and western areas have gradually emerged advantages in the business environment and labor resources, attracting Taiwanese investment to spread across the region. However, the focus of investment is still in the eastern part [10]. Regarding industrial development, Taiwan has entered the service society, and the service industry urgently needs to expand the development space of external demand. The Mainland is in the late stage of industrialization and the early stage of a service society [11]. Therefore, after the signing of ECFA, Taiwan's industrial layout in mainland China presents a trend of optimization both geographically and industrially.

### **3.5. Preferential Policies on Taiwanese Are Proposed**

In February 2018 and November 2019, the Taiwan Affairs Office of the State Council, together with the National Development and Reform Commission and other ministries and commissions, issued several "Measures to Promote Cross-Straits Economic and Cultural Exchanges and Cooperation" (31 Preferential Measures for Taiwan) and "Several Measures to Further Promote Cross-Straits Economic and Cultural Exchanges and Cooperation" (26 Preferential Measures for Taiwan). At present, the Mainland's policy of benefiting Taiwan mainly focuses on the economic and trade field and has obvious unilaterally transferring benefits. For example, it will unilaterally expand procurement from Taiwan and implement trade facilitation measures against Taiwan [12]. In addition, the new preferential measures for Taiwan policy allow Taiwan enterprises to advance westward, which greatly reduced the barrier for Taiwan enterprises to advance western provinces [11]. Therefore, China continues to adhere to the favoring Taiwan policy and tries to promote a common market.

## **4. Constraints on the Establishment of Cross-straits Common Market**

### **4.1. There Are Political Rivalries Across the Strait**

Since the Democratic Progressive Party of Taiwan (DPP) came to power, the existing dialogue and consultation mechanism between the cross-Straits has been interrupted due to its failure to recognize the 1992 Consensus. As a result, it is challenging to promote and implement the relevant agreements already reached, which directly affects the progress of the common market. In addition, in August 2020, the DPP said it would amend the applicable regulations of the "Measures for Permitting Mainland People to Invest in Taiwan" to restrict mainland investment in Taiwan strictly. Therefore, the political confrontation between the two sides has led to the antagonistic development of two sides' relations. Under the background of no political consensus and mutual trust between the two sides, The Taiwan side worries that the close economic relationships between the cross-Straits will lead to Taiwan's economic security problems. Hence, it is not willing to close economic exchanges and contacts between contacts in the cross-straits. In other words, the Taiwan authorities hold a negative



attitude towards constructing the cross-Straits common market and are unwilling to further open their market to the Mainland [13].

#### **4.2. Structural Contradictions Exist in Cross-strait Economic Relations**

Although ECFA has been signed for more than ten years, the unilateral characteristics of cross-strait trade and investment are evident due to cross-strait relations, which leads to the long-term existence of structural imbalance [14]. Firstly, Taiwan's investment in China has grown slowly. Since 2015, Taiwan's investment in the Mainland has decreased year by year and reached the bottom in 2019. Secondly, cross-strait trade growth is sluggish. The growth rate of cross-strait trade has also slowed down due to the slowing growth of Taiwan companies' investment in mainland China. Cross-strait trade topped \$100 billion in 2006, but growth has slowed overall since then. Thirdly, Industrial competition and cooperation patterns failed to form. In the past ten years, the economic status of Taiwan enterprises and the market share of Taiwan products in the Mainland have declined. Except for some industries such as semiconductors, Taiwan's competitive advantage against the Mainland has weakened. For example, from 2005 to 2016, in the fixed asset investment in the electronic information manufacturing industry on the Mainland, the proportion of local enterprises on the Mainland increased significantly from 36.6% to 81.1%, while the proportion of Hong Kong, Macao, and Taiwan enterprises decreased from 22.2% to 7.6%. Mainland companies are also catching up in terms of sales value. The changing situation of industrial competition and cooperation between the two sides is changing the traditional pattern of interests [15]. Fourthly, Cross-strait investment has yet to normalize. Up to now, the Mainland has used about us \$70 billion of Taiwan's capital. However, Taiwan has only allowed Chinese capital to invest in Taiwan since June 2009, and the amount of investment is quite limited, totaling less than \$3 billion so far. The projects that mainland capital can enter into the island are minimal. The approved projects are mainly wholesale and retail and related to communications, catering, plastic products, tourism, and other industries. According to the Ministry of Commerce of The People's Republic of China, as of September 2019, a total of 492 non-financial companies from the Mainland had established centerprises or representative offices in Taiwan with the approval of the Ministry of Commerce, with a record amount of us \$2.674 billion. To sum up, there are structural contradictions in the economy and trade between the two sides, which will restrict the further economic integration of the cross-Straits common market in the short term.

#### **4.3. The Cross-straits Lack Effective Institutional Guarantee**

Although the signing and implementation of ECFA have upgraded the institutionalization of cross-Straits economic cooperation in many fields, ECFA is only partially open to trade in goods, but not fully open, especially in the field of service trade, which the Legislative of Taiwan has not passed. The most significant concession China made in the early days of the ECFA was to temporarily drop demands for cross-strait trade normalization to avoid touching Taiwan's most sensitive agricultural opening. However, the goods deal cannot avoid that issue. Secondly, the scope and process of cross-Straits opening-up. Under WTO rules, both sides of the regional cooperation agreement should open substantive trade (zero tariffs for most goods) within a 10-year transition period. At present, the ECFA agreement has reached a 10-year term. Implementing the follow-up is unavoidable [10]. Therefore, the cross-straits need a follow-up regional trade agreement to ensure that both sides have the institutional guarantee to upgrade the development of the cross-Straits common market.

## 5. Conclusion

### 5.1. Conclusion of Research

This paper mainly researches the restriction factors when the cross-straits jointly establish the market. The common market is an advanced stage of economic integration and development, but at present, the two sides are still in the lower stage of PTA. In addition, establishing a cross-strait common market is an economic means to promote cross-strait economic cooperation and ensure the peaceful development of cross-straits. Therefore, it is necessary to study the restrictive factors of the cross-straits common market, which can improve the establishment of the common market and increase the further integrated development of the cross-straits economy.

At present, the main economic and trade agreement between the two sides is the ECFA signed in 2009. After the signing of ECFA, cross-strait trade volume increased year by year and reached its peak in 2020. Meanwhile, Taiwan's trade surplus with China reached \$140.52 billion. In addition, Taiwan's investment in the Mainland began to multiply after the signing and peaked in 2015. Although investment has declined in recent years, it still accounts for 33% of Taiwan's total foreign investment in 2020. In addition, due to many restrictions on Taiwan's investment in the Mainland, mainland investment in Taiwan decreased compared to 2014 but still reached \$1.59 billion. Additionally, Taiwan's investment in the Mainland has shown optimization. In the region, Taiwan enterprises appeared to invest in the west of the trend. In terms of industry, Taiwan's service trade industry can complement the manufacturing industry of the Mainland. Finally, the Mainland has introduced several preferential Taiwan policies to attract Taiwan enterprises to invest in the Mainland and encourage them to invest westward.

Based on the above analysis, there are three main restricting factors between the two sides. First, there are political rivalries between the two governments. The DPP and the mainland governments have different political views, especially in the "1992 Consensus". Secondly, there are structural contradictions between the two sides in economy and trade. Taiwan's investment in the Mainland has been declining year by year in recent years, although the Mainland is still Taiwan's largest overseas investment destination. And while total cross-strait trade is still growing, the pace of growth has slowed. Also, the original complementary's cross-strait economic and trade structure gradually changed into a competitive system. This is because as China's economic power grows, the trade areas between the two sides begin to overlap, and Taiwan's competitive advantage diminishes. Additionally, cross-strait investment has not been normalized, and the Mainland is still in a position of unilateral openness. Finally, the two sides lack institutional guarantee. Although the ECFA has been signed for a decade, the two sides have not yet reached a reciprocal opening, and the service trade agreement is still on hold. Therefore, a new institutional arrangement is urgently needed to ensure the steady development of a cross-strait economy and trade.

### 5.2. Limitation

Although this paper tries to analyze the restrictive factors of establishing the cross-straits common market, there are still a series of limitations. First of all, this paper mainly discusses the establishment of a cross-strait common market from the perspective of mainland China without considering the perspective of Taiwan. Taiwan authorities still play a significant role in establishing the cross-Straits common market. Secondly, this paper mainly analyzes the restrictive factors from an economic perspective. Although some political elements are considered, it does not make a systematic analysis. Thirdly, this paper does not consider the influence factors of countries outside the region. For example, during the China-US trade war, the US imposed tariffs on Chinese exports to the US, which increased the cost of Taiwan-invested enterprises on the Mainland's which exports to the US, thus affecting the



trade of intermediate products such as components and raw materials between enterprises across the straits [14].

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